VZCZCXRO5192
PP RUEHDE RUEHDIR
DE RUEHDH #0228/01 2431438
ZNY CCCCC ZZH
P 311438Z AUG 09
FM AMCONSUL DHAHRAN
TO RUEHC/SECSTATE WASHDC PRIORITY 0267
INFO RUEHZM/GCC C COLLECTIVE
RUCPDOC/USDOC WASHDC PRIORITY 0004
RUEHRH/AMEMBASSY RIYADH PRIORITY 0244
RUEHJI/AMCONSUL JEDDAH PRIORITY 0049
RUEHBJ/AMEMBASSY BEIJING PRIORITY 0004
RUEHDH/AMCONSUL DHAHRAN 0349

C O N F I D E N T I A L SECTION 01 OF 03 DHAHRAN 000228

NOFORN
SIPDIS

DEPT FOR NEA/ARP JOSHUA HARRIS AND JEREMY BERNDT

E.O. 12958: DECL: 8/31/2019
TAGS: ECON ENRG EPET PGOV SA CH
SUBJECT: SAUDI ARAMCO-DOW CHEMICAL $24 BILLION PETROCHEMICAL PROJECT
MOVING FORWARD

REF: A. A. 07 RIYADH 1006
¶B. B. DHAHRAN 74

DHAHRAN 00000228 001.2 OF 003

CLASSIFIED BY: Kevin Kreutner, Acting Consul General, EXEC, DOS.

REASON: 1.4 (b), (d)

SUMMARY

¶1. (SBU) Saudi Aramco project finance managers confirmed that the $24 billion joint venture (JV) with Dow Chemical is moving forward, despite the economic crisis. In return for access to cheap, discounted feedstock (primarily ethane and naphtha), Dow is sharing with Aramco a number of the "crown jewels" of the chemical company's most advanced technology. Although many of the Dow-Aramco chemical products will not directly compete with those of the national petrochemical giant SABIC, both companies will be vying for scarce feedstock allocations from the Ministry of Petroleum and Minerals (MinPet). The large integrated refinery and petrochemical complex's products will be marketed towards the GCC and Asia. END SUMMARY.

DOW-ARAMCO PROJECT MOVING FORWARD

2.(SBU) Saudi Aramco's $24 billion dollar JV with U.S.-based Dow Chemical will reportedly result in one of the largest single phase petrochemical complexes in the world, at Ras Tanura on the Persian Gulf coast a few dozen miles north of Dhahran. (NOTE: Ref A provides detailed information on the specifics of the Dow-Aramco project. Cost estimates of the JV have not been finalized, but range from $20 to $27 billion. END NOTE.) However, the global economic crisis has hit the petrochemical industry hard. According to a recent Saudi bank report, approximately $27 billion worth of petrochemical projects were put on hold in Saudi Arabia this year alone. In addition, in December 2008, a $17 billion joint venture between Dow and Kuwait's state-owned Petrochemicals Industries Company unexpectedly collapsed. The proceeds from the Kuwaiti deal were slated to pay down debt resulting from Dow's recent acquisition of Rohm & Haas, a petrochemical firm. This perfect storm has

raised industry speculation about Dow's ability to raise its share of the substantial up-front capital investment required for the Saudi venture.

¶3. (C/NF) In an August 24 meeting with EconOff, a Saudi Aramco project finance manager said that both Aramco and Dow had already "sunk $500 million that I can tell you about [into the project]." "The project will get done, there is too much on the line for both [Dow and Saudi Aramco]," he said, adding that both Aramco and Dow are fast approaching the point where too much money has been invested to "walk away" from the deal. In an August 26 teleconference, Lisa Schroeter (strictly protect), Dow Chemical's Director for International Policy, told EconOff that approximately 900 Dow employees are already working on the JV, indicating Dow's seriousness to carry out the project.

DOW GETS CHEAP FEEDSTOCK, ARAMCO GETS HIGH-END TECHNOLOGY

--- ------------

¶4. (C/NF) Saudi Arabia is a significant player in the petrochemical industry; it currently accounts for 7% of the global supply of basic petrochemicals, and its share is growing. The key to the Kingdom's success has been access to heavily discounted gas feedstock, primarily ethane, which sells at $0.75 per million British thermal units (Btu). The consistent flow of feedstock at a cheap fixed price is particularly attractive to an industry with huge capital outlays that often require several decades to see a return on the initial investment. Schroeter confirmed this when she said, "Ras Tanura is key because the fixed price [of feedstock] is reliable."

DHAHRAN 00000228 002.2 OF 003

¶5. (C/NF) According to the Aramco project finance manager, in return for the cheap ethane and naphtha feedstock allocations, Dow will share the "crown jewels" of the chemical giant's technological know-how. These downstream technologies were specifically chosen because they will maximize job creation in the Kingdom. However, the final set of technologies agreed upon had to be approved by MinPet before the JV would be granted a feedstock allocation. The gate keeper to the gas allocations at MinPet is Prince Faisal bin Turki Al-Saud (Ref B). In the end, the prince granted the initial ethane allocation, though this process must be renewed annually until a final investment decision is made and construction of the complex begins.

ARAMCO STEPPING SQUARELY ON SABIC'S TURF

¶6. (C/NF) Notwithstanding Aramco's $10 billion Petro Rabigh JV with Japanese powerhouse Sumitomo Chemical on the Red Sea coast, the Dow project is Aramco's biggest and boldest move into the petrochemical market -- a domain largely dominated by the Kingdom's other major national company, Saudi Basic Industries Corporation (SABIC). In a meeting earlier this year, Aramco CEO Khalid al-Faleh said that in most cases the Dow-Aramco JV would not be going "head-to-head" with SABIC, but that a "little competition" is always good. SABIC executives have made similar comments. Hamad al-Madi, General Manager for SABIC Eastern Province, said that they view the Dow JV as a "challenge, not an obstacle" and that a "monopoly kills the economy."

¶7. (SBU) However, despite the polite commentaries from Saudi Arabia's two largest state-owned companies, the petrochemical industry is competing for the same precious feedstock: gas (ethane and methane) and liquids (naphtha, butane, and propane). In Saudi Arabia, this competition is fierce due to the heavily discounted price of the feedstock, particularly the increasingly scarce ethane gas. Whereas SABIC has historically invested heavily in ethane-based chemicals, the Dow-Aramco JV will use a more balanced feedstock mix of ethane, methane, naphtha and natural gas liquids. Nevertheless, the Dow-Aramco JV will certainly increase the demand for the Kingdom's scarce hydrocarbon resources.

DOW EYES THE CHINESE MARKET, WARY OF POLITICAL FALLOUT

--- ----------

¶8. (SBU) With Saudi Arabia's rapid ascent as a major petrochemical producing nation, the Kingdom is increasingly in competition with China, which is also a major petrochemical player. Whereas Saudi Arabia's comparative advantage lies with cheap feedstock, China has cheap (and skilled) labor and is closer than Saudi Arabia to their shared destination market, Asia. Recently, tensions have surfaced with Chinese officials accusing SABIC of "dumping" chemicals on the Chinese marketplace.

¶9. (C/NF) Dow's Schroeter told EconOff that the Aramco JV will have two primary target markets: the GCC and Asia. (NOTE: Schroeter made this point to highlight that the Aramco JV would not compete directly with the domestic U.S. petrochemical marketplace. END NOTE.) She also voiced some concern about the ramifications of China's anti-dumping accusations in the Sino-Saudi commercial relationship. However, as Saudi Arabia's share of foreign oil sales to China continues to increase (it reportedly was the country's largest supplier of oil in July, overtaking Angola), we expect commercial ties between the countries remain strong.

DOW AND ARAMCO VOICE VISA CONCERNS

DHAHRAN 00000228 003.2 OF 003

¶10. (SBU) Reflecting similar concern raised by Dow employees in Ref A, both Schroeter and Aramco officials were apprehensive about difficulties in securing U.S. business visas for Saudi nationals needing to travel to the United States. Due to long visa appointment wait times and Security Advisory Opinion processing times, EconOff recommended that Aramco and Dow work early to identify the Saudi nationals who will need to travel to the U.S. for the JV. Operating within the consular section's guidelines, the Consulate will remain flexible to help facilitate this strategically important multi-billion dollar U.S.-Saudi joint venture.

COMMENT

¶11. (C) Competition between Aramco and SABIC will intensify as the Saudi national oil company giant intensifies its presence in the petrochemical sector. The decision for Aramco to move into petrochemicals was a profit-driven business decision. Unlike the refining sector, which requires large, risky investments with thin profit margins, integrating a refinery with a petrochemical complex allows for more value-added products, thereby spreading the initial capital costs over a broader product line with higher margins. Although this move makes economic sense, an important strategic decision such as this must also receive the blessing from the highest levels of the Saudi government. Therefore, the decision for Aramco to compete with SABIC in the petrochemical industry is just as much a political decision as it is an economic one. Nevertheless, Post believes that the two giant government-controlled firms (the SAG owns 100 percent of Aramco and 70 percent of SABIC) will co-exist and prosper in the Kingdom, as the SAG would not let either firm fail or squander profits fighting the other over the spoils of the Kingdom's patrimony. END COMMENT.
KREUTNER